ALGOMA STEEL

Annual Meeting of Shareholders

April 19, 1983

Address

by

John Macnamara

Chairman and Chief Executive Officer

and

Peter M. Nixon

President and Chief Operating Officer

THE ALGOMA STEEL CORPORATION, LIMITED

ANNUAL MEETING ADDRESS

In my annual address to shareholders a year ago, I remarked that the North American economy was in a recession of indeterminable proportions. Little did I realize that the combined Canadian and United States steel industry would operate at 50 percent of capacity and many major North American integrated steel companies would incur losses for the first time since the depression of the 1930's. As the year progressed, Algoma's quarterly operating rates steadily declined to a low of 36 percent of capacity in the fourth quarter and the Corporation suffered its first annual loss since the company was incorporated in 1935. The previous three years of successive record earnings made the magnitude of the 40.4 million dollar loss even more difficult to accept.

Algoma's combined advantages of captive raw materials, modern manufacturing facilities, versatile rolling mills, continuous casting capability, computerized systems, improved customer communication and service, and overall improved union/management relations, were not sufficient to overcome the sharply lower volume, the less profitable product mix, and the impact of inflationary cost increases that could not be offset by price increases.

Unlike other industrialized countries, Canada maintained a reasonable level of steel production during the seventies. But the North American steel industry experienced more than just a cyclical downturn in 1982 and steel production in the United States and Canada dropped drastically compared with other major steel producing countries. Algoma was particularly hard hit because its product mix was so susceptible to the deferrals or cancellations of major capital projects and the precipitous drop in spending on oil and gas exploration and development.

To compound the problem of lower domestic demand, much of the record tonnage of plate and wide flange shapes imported into Canada in the latter half of 1981 was still in inventory at the beginning of the year and satisfied many customers' requirements for a good part of 1982. Since we believe a high proportion of this tonnage entered Canada at dumped prices, Algoma has initiated anti-dumping proceedings

to curb the unfair importation of plate and wide flange shapes into Canada. A preliminary determination is expected to be made by Revenue Canada next month and a positive determination should reduce imports and provide Algoma with the opportunity of operating at higher rates. While we expect the support of government in prohibiting foreign steel producers from contravening Canada's trade laws, we recognize Algoma's responsibility to supply Canadian customers on a reliable basis with products of competitive quality to those that could be sourced offshore.

The total collapse of the oil country tubular goods market was especially damaging to Algoma. The suddenness with which this occurred is best illustrated by the fact that monthly gross earnings from tubular sales fell from a record high to a loss in only eight months - March to November. This was the first loss on this product since the tube mill was acquired in September 1971. Even now, as much as twelve months supply of oil country tubulars is estimated to be in inventory in the United States and with the uncertainties surrounding oil and gas pricing and consumption, drilling activities in the United States and Canada are forecast to be well below prior years. Unless there is unforeseen change, Algoma's seamless production is expected to remain considerably below capacity throughout 1983.

The Federal Government's announced intention to extend Canadian customs jurisdiction to the outer limits of the continental shelf will, when enacted, provide Canadian producers with protection against unfair competition. Under the existing 12-mile limit, Algoma is obliged to offer seamless tubulars at unprofitable prices in order to compete with countries which are supplying steel into international waters at heavily discounted prices. This legislation should provide protection against dumping and ensure a high degree of Canadian content in steel used for offshore oil and gas exploration and development.

Another factor contributing to Algoma's lower 1982 shipments and reduced earnings was the sharp decline in our exports to the United States. Steel demand in the U.S. was severely depresssed and domestic and import prices were heavily discounted. Algoma could not match competitive prices without being in violation of the U.S. anti-dumping laws. While U.S. sales

are extremely important to Algoma, it is not our intention to sacrifice long term business relationships with major U.S. customers for the sake of short term gain.

Algoma's 1982 cash shortfall, after providing for capital expenditures of 185 million dollars, was 219 million dollars. Revenues declined at a faster rate than spending could be curtailed and it was necessary to refinance short term bank borrowings through the placement of 50 million dollars Canadian and 100 million dollars U.S. of new long term debt. This increased Algoma's debt to 34 percent of total capitalization at December 31, 1982 which, while not unusual in the steel industry, is nevertheless a deterioration in the Corporation's financial position. We are examining various options to improve our financial position but we recognize that top priority must be given to cash generation from operations.

Long term debt will continue to increase in 1983 through drawdowns against the previously unused 250 million dollar project financing arranged for the construction of the new seamless tube mill. About 200 million dollars was spent on this mill without borrowing against this source of funds.

As previously announced, construction on the new mill has been suspended until there is a turnaround in the demand for oil country tubular goods. However, about one-half of the 50 million dollars in total capital expenditures planned for 1983 is for previously ordered tube mill machinery and equipment which should all be on site by mid-year. Engineering and marketing studies are in progress to determine the cost and feasibility of finishing a section of the mill to further process pipe rolled on the existing seamless tube mill. This would extend Algoma's tubular product line to include the full size range of the new mill and begin phasing in the new mill over a period of time to parallel expected recovery and growth in the tubular market.

Hindsight would indicate that the decision in 1980 to begin construction on a new seamless tube mill was poorly timed. Naturally, we would not have proceeded had we foreseen the negative aspects of Canada's 1980 National Energy Program, the excessive inventories which were accumulated in the United States during 1981 by major oil companies and distributors, and the

international oil glut brought on by the recession and energy conservation. The recent reduction in world oil prices has resulted in further suppression of North American oil and gas drilling programs. We are confident, however, that in the long run, Algoma will benefit from this modern, world class facility and we will be one of two preferred North American suppliers of seamless tubulars - the other being a mill of similar design under construction in the United States.

It is regrettable that in the United States and Canada the ultimate virtue and desirability of long term oil self-sufficiency has given way to the perceived short term economic advantages of purchasing rather that producing oil requirements. The vulnerability to foreign oil sources appears to be forgotten. It seems ludicrous that literally billions and billions of dollars - over 5 billion in Canada alone in 1982 - should be spent on crude oil imports when we have the potential for oil self-sufficiency. This outflow of funds should increase as the economy strengthens and demand for oil and natural gas continues to rise above domestic production capacity.

We believe Canada's National Energy Policy should not only focus on energy self-sufficiency but should also be directed toward a strategy which would encourage overall development and processing of Canadian energy resources. Algoma will play a part in this development through our concentration on products which are essential to the construction, transportation and energy sectors.

The recession is still with us and continues to curtail steel production throughout the world, except in the developing countries. Today, and most likely for several years to come, the fear of a steel shortage has given way to the reality of excess raw steel capacity. Only in developing countries such as Korea, Brazil, China, Taiwan, Mexico and India, is new steel capacity planned or under construction. This is in direct contrast to industrialized countries where declining domestic demand, high employment costs and inefficiencies associated with older, less productive equipment have resulted in plant shutdowns, mergers, product rationalization and slow but continuous shrinking of raw steel and rolling mill capacity.

The world is awash with excess metallurgical coal, iron ore, steelmaking and rolling mill

capacity. It is ironic that only 711 million net tons of raw steel were required to satisfy world consumption in 1982 when in 1973 and 1974, 768 and 775 million tons, respectively, could hardly satisfy demand. Forecasts made only five years ago by authoritative sources indicated world demand would reach one billion tons by 1985. More recent forecasts now suggest that 825 million tons is a more likely figure for 1985 and the one billion mark may not be required by the end of the century.

The magnitude of the existing excess capacity is dramatized by the decline in raw steel production last year in the United States. In September 1981, the 1982 outlook for raw steel production in the United States was approximately 132 million tons as reported to the International Iron and Steel Institute but only 73 million tons were produced from a capacity of 150 million tons. Canada estimated 18.7 million tons of raw steel in 1982 but produced only 12.9 million - so much for forecasts.

It is becoming more and more evident that Algoma must concentrate on producing and selling a select range of specialized rolled steel products at prices and quality which are competitive in North American markets. This dictates that we cannot continue to produce the myriad of steel shapes and sections that we have in the past. The Corporation's total assets must be dedicated to ensuring that Canadian steel consumers will look to Algoma as their preferred supplier of plate, wide flange shapes, wide hot rolled sheet, rails and seamless tubulars. We can do little to create a market for these products but once the market is there, we must and will do everything possible to maintain or improve our market share.

I would like you to hear directly from Peter Nixon, our President and Chief Operating Officer, as to how we intend to go about competing in the difficult markets of the 1980's.

Thank you, John.

Planning for recovery must start with the realization that while markets for Algoma's products will increase from present low levels, the North American marketplace will continue to be oversupplied by domestic producers and by imports. No Western world steel producer

can expect to market products in the 1980's without being fully competitive in quality, service and price. These are not new or novel criteria but they have taken on new meaning for Algoma in this changed market environment of the eighties.

We are a major Canadian steel company and that is not going to change. We have no intention of moving into some new line of business unrelated to steel. But in today's competitive steel world we must build on our strengths and become even better at what we do.

Our captive coal and iron ore operations have been an important part of Algoma and that will continue. Sale of raw material reserves or assets, such as has taken place in some North American steel companies, is not in Algoma's plans. We are producing coal for sale to others and we will continue to do so but only where profits can be generated without jeopardizing metallurgical coal reserves required for Algoma's use. The main thrust at our mines and preparation plants must be to provide higher quality raw materials to the Steelworks at lower costs.

The absolute dedication to low cost production that begins in raw material operations must extend throughout the Corporation. Algoma has traditionally been a cost efficient steel company, but the 1980's have brought increased competition from North American and offshore producers that are also dedicated to low cost production. Past performance is not good enough in an oversupplied market where prices are going to remain very competitive. The survivors are going to be the low cost producers - and we intend to be one of them.

In the crowded marketplace of the 1980's we must, as never before, give the customer what he wants, when he wants it, at a price he is willing to pay. "Make it right - on time - the first time" must increasingly be the creed of every Algoma employee. This will provide the opportunity for even more aggressive salesmanship in competing for the orders that will keep our people working and provide a satisfactory return to our shareholders.

What I have said so far identifies what has to be done, but I've said very little about how it will be achieved. The answer is good management, a responsive work force, hard work and

continuing change. Change in priorities, change in technology, change in equipment and change in procedures.

Let me give you examples of the changes that will be required and how they can be achieved. It is perhaps appropriate to start with changes in priorities.

There has traditionally been a temptation for steel producers, including Algoma, to "get out the tons". The focus in continually expanding markets has been to get out those incremental tons which have been so profitable. Product lines have been retained and older production units have been kept in operation as long as they contributed shipment tons and overall corporate results were satisfactory.

The announced shutdown of the bar and strip mill and the ball mill is recognition that Algoma's priorities are changing. These mills were major contributors to both tons and profits over many years but they can no longer compete and earn their way. The tons could still be produced - but not the profits.

We will have to make similar decisions on other older facilities and concentrate on reinforcing Algoma's basic strength as a low cost plate, sheet, wide flange, rail and seamless tubular producer in good or bad markets. These are the Algoma products that will compete in the markets of the 1980's but each of them must earn its way with acceptable profit margins. There can be no free rides for products that provide tons but don't contribute their fair share to earnings.

The need for change in technology is not new. The steel industry has been going through evolution if not revolution for the past fifteen years. Mini-mills, computerization, raw material improvement, upsizing of production units and, most importantly, continuous casting have been key components of technological change.

Algoma has been part of this changing technological pattern.

— We pioneered basic oxygen steelmaking production of high carbon steel and were the first in the world to continuously cast beam blanks
— We have made large strides in improved raw material quality

- We are a North American leader in process control computer application
- We have built new large facilities like No. 7 blast furnace, No. 2 basic oxygen steelmaking plant and the new slab caster
- We've added improved product capability with the plate and tube heat treating units

and

- Our new seamless tube mill will be a prime example of world class technology.

But dollar constraints have forced prioritization and restricted Algoma's ability to introduce other technological improvements. We know that we must expand and improve our continuous casting capability. We recognize that No. 1 steelmaking shop must be modernized or replaced. We appreciate the importance of adapting new steelmaking technology to product improvement. There is no shortage of ideas for technological change, but capital dollars are, as always, in limited supply. Available funds must be even more carefully allocated in the 1980's to achieve the greatest possible impact from each expenditure. Our capital must be directed toward improved quality and cost reduction and not toward additional raw steel capacity.

We can expect product demands of the 1980's to move quality requirements beyond the capability of existing equipment. We must use the facilities that we have to the absolute best advantage but equipment changes and improvements will be necessary. I have already talked about changes in steelmaking and continuous casting and to these must be added modifications to rolling mill and finishing equipment - particularly as related to potential improvements in cost efficiency and product quality.

Demand for more sophisticated products has already resulted in the installation of new tube and plate heat treating equipment. A third slab reheat furnace and the new coil box will improve our strip mill yield, quality and production capability - and potential benefits from further processing of strip products is recognized through the recently announced association between Algoma and Sonco Steel Tube Limited.

Algoma is one of the few, if not the only, North American steel producer, that has not had a captive outlet for its strip mill products. The Sonco arrangement will provide Algoma with

this missing link and with a future option to acquire an ownership position in Sonco and its hollow structural products and welded tubulars which fit naturally with Algoma's wide flange shapes and seamless tubulars.

The need for improved product testing equipment at Algoma has been recognized and changes are already underway to meet the more sophisticated customer demands. Quality assurance has always been important but today's standards are even more demanding than in the past. Practices that were good enough yesterday are not good enough today and they will be even less acceptable tomorrow.

"Just in time delivery" is another new customer demand and there will be no exceptions for Algoma or any other supplier. Geography makes it more difficult for Algoma to meet short lead time deliveries but we must compete. We are developing new shipping procedures to satisfy these more stringent market requirements.

And so from raw material production to customer delivery, Algoma is changing.

The year 1982 has been a terrible shock to the steel industry and to Algoma. We thought we were doing a pretty good job and that we stacked up well on comparative performance. But we must accept that standards have changed and performance must be much higher in this competitive environment. We cannot and must not assume that we will be back to "business as usual" in this year, next year or any other year.

Compared with our competition from Japan or from the developing countries, we have high wages and salaries. The salaries of Algoma employees have been restricted for some time and work sharing has reduced the takehome pay of many salaried people. We recently proposed to representatives of our United Steelworker of America local union that certain tonnage related remuneration and contractual future wage increases be deferred and accumulated for payment in 1985. That proposal was rejected and it was made clear in the union's response that neither concessions nor deferrals of existing contractual commitments would be considered. Canadian steelworker wages and benefits are second only to those in the United States where significant wage reductions have recently been negotiated. We must find ways to reduce the employment costs in our steel products.

High employment costs - and I'm talking of both union and management costs - demand equally high standards of performance. If we expect to be paid higher rates, we must earn them and the only way we can earn them is through superior performance in the marketplace, reduced costs and improved profitability. If this means changing attitudes - then attitudes will have to change.

We have seen a tragic decline in employment at Algoma in 1982/83. I say "tragic" because that's exactly what it has been to the many people who have been out of work. Those who have had their earnings reduced have also suffered. I wish I could tell you today that everyone will soon be back to work but, unfortunately, that is not going to happen. Even when we return to higher levels of production we will not have as many employees as we did in 1981. We simply cannot afford to return to previous employment levels if we are to achieve the productivity performance necessary to compete in the 1980's.

Throughout the Western world, increasing steel competition has brought with it demands for improved productivity. Productivity of capital so that dollars are only spent where they will achieve tangible results. Productivity of materials so that more product is shipped for every ton of raw materials used. And productivity of people so that every worker, whether management or union, fully justifies through his or her efforts the wage that he or she is being paid. Algoma is part of this productivity contest.

At all levels in Algoma's organization the question has been asked "Why must we change?". The answer is because the economy has changed, the industry has changed and our markets have changed and we must also change or be left behind. From top to bottom the Algoma focus must be on recognizing opportunities for innovation and improvement, and implementing changes. You only have to read the annual reports of other steel companies to see that we are aiming at a moving target. Other companies are improving - and so must we.

We have not been standing still. Performance in each area of the Corporation has been under close scrutiny and improved results have been achieved. They have not yet been translated into profits because of the low demand for our major products and suppressed steel prices, but our

profit potential has increased. We must look now to continuation of this trend so that we can move to new levels of productivity improvement and cost reduction.

We are in for a more difficult and challenging period than has been experienced at any time since the 1930's. But we have the knowledge, the determination and the capability of meeting that challenge. Our commitment must be not only to survive these troubled times but to be once again a leader in the years ahead.

Thank you, Peter.

Effective use of capital, optimum use of existing facilities, greater productivity, cost reduction, assured quality, product rationalization, aggressive selling, on time delivery and changing attitudes constitute the foundation upon which we will build Algoma's future.

The benefits of changing our attitudes to resolving problems have been clearly demonstrated by the remarkable progress that has been achieved in making Algoma a safer place to work. A high degree of co-operation, trust and understanding between union and management has resulted in the introduction of a unique joint health and safety program which was highlighted at the Industrial Accident Prevention Association annual meeting in Toronto last week. More importantly, the steelworks accident frequency has been cut in half since 1980 and the improved results are continuing. We have come a long way but there can be no end to our efforts to reduce accidents and improve the environment in which our employees work.

There are positive signs that the recession has bottomed out, but demand for most of Algoma's major product lines is lagging behind the upward trend in orders for hot and cold rolled sheet destined for consumer-oriented products such as automobiles and appliances. This sudden surge in sheet orders could be short lived if car sales level out or decline and inventories are fully replenished. There has been some improvement in orders for wide flange shapes but demand for plate and seamless tubulars remains at very low levels. The combined backlog for all of Algoma's products is currently less than one-half of 1981 backlogs.

Algoma's first quarter raw steel production increased to 46 percent of capacity compared

with 36 percent in the fourth quarter last year. Second quarter production is expected to rise slightly above 60 percent of capacity, but prices and product mix continue to be unfavourable. Shipments will include semi-finished products which generate cash and create employment but contribute little to earnings.

First quarter sales were 169 million dollars compared with 160 million dollars in the fourth quarter last year. But this is still only half of 1982's first quarter sales of 321 million dollars. We are estimating a first quarter loss of 33 million dollars compared with the 38 million loss in the fourth quarter last year and net earnings of 35 million dollars in the first quarter of 1982. The first quarter results are expected to be published on April 26.

It is apparent that Algoma's operating rates will remain at low levels and a loss is expected in the second quarter although not as great as the first quarter loss. This dictates that we must continue to operate in a survival mode and conserve cash to the greatest degree possible. In the Canadian operations, there are approximately 3,900 union employees on indefinite layoff and the majority of salaried personnel remain on a four day work sharing program. Since the beginning of 1982, management forces have been reduced by 240 employees and further reductions will occur at mid-year. Total employment in the Cannelton coal mining operations in West Virginia has been reduced even more severely to conform to the cutback in coal production.

Our employees and shareholders have borne the hardships of a disastrous 1982. We regret the layoffs, the reductions in takehome pay and the decision to omit the first quarter common share dividend. For many of us, this is the first serious recession - bordering on depression - that we have experienced in our working careers and it is difficult not to be caught up in doom and gloom.

However, we are confident that steel markets will recover and we will emerge from this recession wiser, more experienced and better equipped to deal with the future. Algoma will have lost two years of growth and prosperity but we will be a more efficient and better managed company.

We still have severely depressed market conditions to overcome during the balance of this year as we do not expect to see a substantial improvement in demand until 1984. We will require the continued confidence and full support of our employees, our customers, our suppliers and our shareholders. With that support and a recovery in steel markets, we will put this difficult period behind us and once again demonstrate that Algoma can produce results of which all of us can be justly proud.